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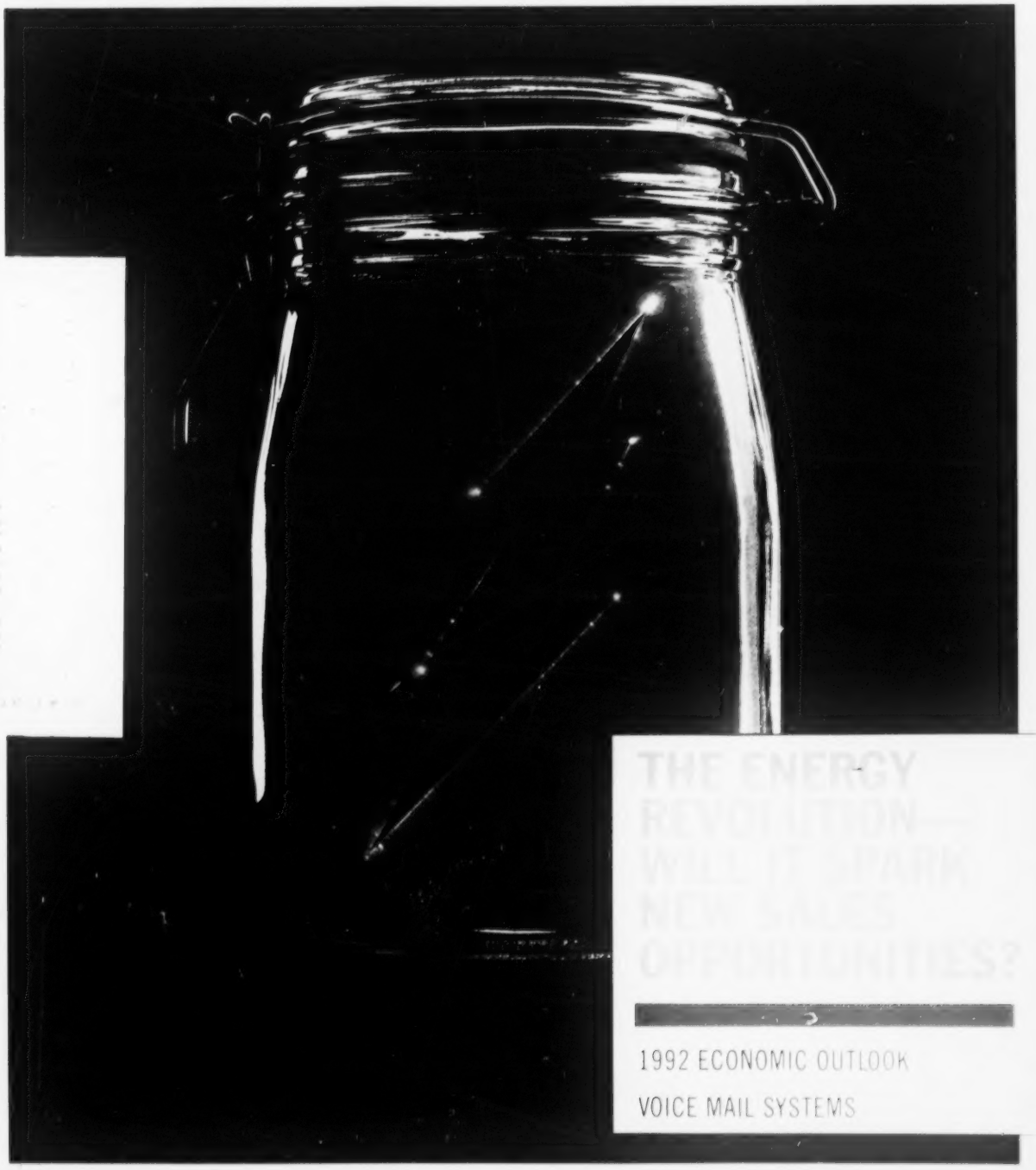
ELECTRICAL WHOLESALING



THE ENERGY REVOLUTION— WHERE ARE THE NEW SALES OPPORTUNITIES?

1992 ECONOMIC OUTLOOK

VOICE MAIL SYSTEMS

VOLUME 72
NUMBER 12

ELECTRICAL WHOLESALING

DECEMBER
1991

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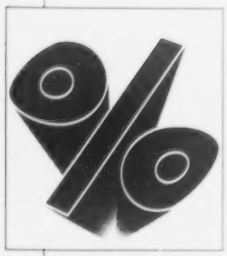

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Al Francekevich

ELECTRICAL WHOLESALING

Chief Editor: Andrea J. Herbert

Executive Editor: Jim Lucy

Art Director: Jacqueline A. Sirvio

Associate Editor: Dean Holstein

Assistant Editor: Lance Ulanoff

Contributing Editors: Dale E. Funk, Timothy Kasen

Contributing Authors: Robert Footlik, Ron Friedman, Pat Gill, Gordon Graham, John J. McCarthy, James B. Newton, Bill Novak, Dr. Don A. Rice, William H. Younger

Special Assignment Writers: Carolyn Brown, Brendan Read

Directory of Electrical Wholesale Distributors: Bernadette Sabatino

THE PUBLISHER'S NOTE

Most people refer to ELECTRICAL WHOLESALING's December issue as our "Outlook Issue," because each year it contains an article that analyzes how the economy will likely affect electrical distributors. This issue does exactly that, with a straight-to-the-point article by *Fortune* magazine economist Joseph Spiers.

But we try to offer much more, and I think Chief Editor Andrea Herbert and her staff have assembled a remarkable package for you in this issue. Some highlights:

"Forecast 1992," page 51. Besides the overall economic outlook, author Joseph Spiers identifies which of your customers are likely to grow next year.

"Remembering 1991," page 45. Executive Editor Jim Lucy does a great job summarizing key industry developments and identifying the sales opportunities they create for you.

"Bottling energy savings," page 41. Associate Editor Dean Holstein gives 10 practical ideas for cashing in on the boom in energy-saving equipment.

There's also a special advertising section where top electrical manufacturers show how their companies are poised to help you find every scrap of business that's out there. It's called "View From the Top," and begins on page 17.

This has been a tough year for most of us in the electrical industry. At ELECTRICAL WHOLESALING, we're dedicated to helping you succeed despite these challenging times. We believe issues like this will help you do just that.

Rich Hathaway

RICH HATHAWAY, Publisher

Group Vice President: Eric Jacobson

Group Publisher: Richard A. Hathaway

Associate Publisher/ Editorial Director: Thomas F. Preston

Advertising Sales Manager: E.F. (Ned) Camuti

Director of Marketing: Joseph Turco

Corporate Circulation Director: Sandra Stewart

President: R.J. Hancock

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FORECAST 1992

ALL EYES ARE ON THE ECONOMY—AND THE TURNS IT MAY HAVE IN STORE—IN THE YEAR AHEAD.

■ However bad the economy was in 1991, it was by no means hell—hell was 1974-75 when OPEC unleashed itself on the world; hell was 1981-82 when the unemployment rate topped 10%, the prime rate was 20% and the U.S.'s manufacturing base crumbled. Today, energy prices are modest and don't threaten to spike, the unemployment rate is under 7%, interest rates are relatively low and U.S. manufacturing has become a lean, mean export machine.

But all the improvement is small consolation to businesses that are struggling today, worrying that things won't get better. It's the fear of the future, the pessimistic mood of business and consumers, that is so different now than in the past, when the immediate conditions were worse. It's not hell, all right, but it's a kind of purgatory— uncertainty without end. It didn't start with Iraq's invasion of Kuwait, which triggered the recession itself through soaring oil prices and plunging consumer confidence. It started a year before that when the economy started to just creep along. So we've been in this purgatory for two and a half years, even though the actual recession may have lasted less than a year.

In the face of this uncertainty, businesses slashed employment in the fall of 1990 and the early months of 1991, making it yet more difficult for fearful consumers to buy much. Since the economy started showing tentative signs of life in the spring, businesses have hired at only a very halting pace; and they have continued to cut their inventories.

By Joseph N. Spiers

The author is an Associate Editor and Economist for Fortune *magazine.*

Fortune's economists believe hiring will pick up gradually and inventories will grow enough to boost the economy about 3% in 1992. That's not a bad growth rate on average, but it's only half the rate of a typical recovery. Given today's glum mood, why expect even half a loaf? Exports will play an important role. Since getting their act together in the mid-1980s, American manufacturers have boosted productivity sharply, more so than those in any other major country except Japan. Costs are under control and prices are highly competitive in world markets.

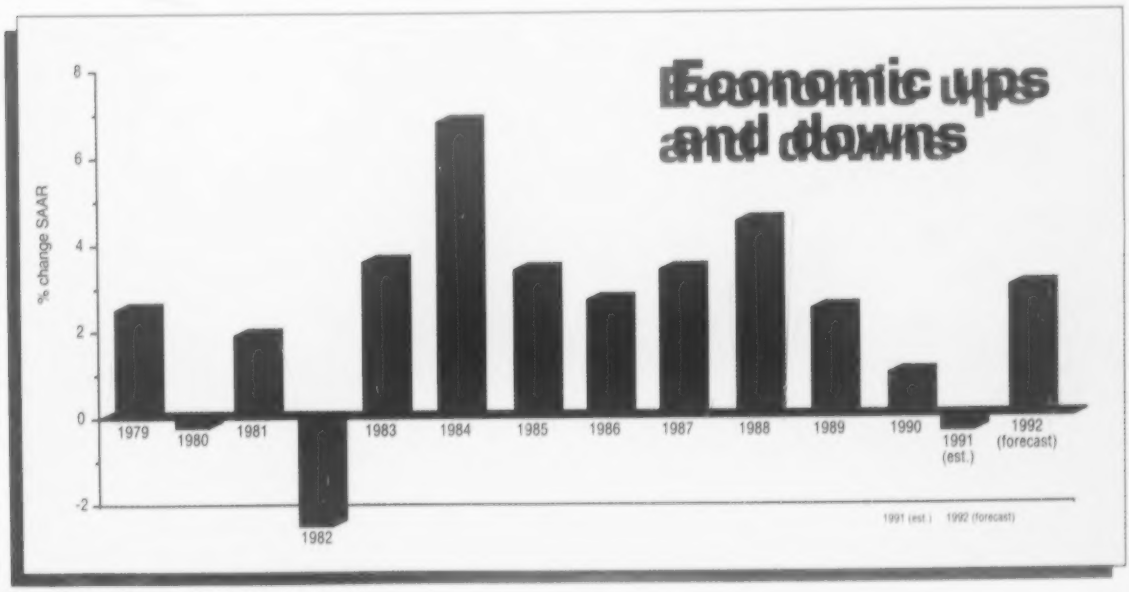
Construction of single-family homes will also provide a lift to demand in 1992. Mortgage rates are the lowest they've been in a decade and a half. And builders realize that people don't want to pay for a Jacuzzi anymore, so they're developing less expensive models. On the cost side, then, things look good for potential buyers. On the demand side, job worries are, of course, a major impediment. But only a tiny fraction of the population buys a house in any given year. With financing costs low and prices attractive, enough buyers should step forward to support an increase in home building. Shoring up demand will be a continuing increase in buying by single people and unmarried couples. At the same time, a jump in births in the last few years to married women may stimulate some demand for new housing as couples seek more space and amenities for their growing families. *Fortune* predicts a nearly 20% rise in single-family housing starts in 1992. That looks good, and would of course be welcomed by electrical wholesalers. But don't forget that the expected increase is from a depressed base. The predicted number of starts next year—990,000—would fall well below the level of activity in the late 1980s, in part because builders will continue to have difficulty getting bank loans.

Apartment and condo construction could show a small gain in 1992, but that's simply because starts in 1991 fell so low, to an estimated 180,000, the lowest on the record, which stretches back to the 1950s. The overhang of tax-shelter-inspired apartment and condo complexes remains a serious problem. So does the relatively small number of people entering their twenties, the prime renting years. Any rise in construction in 1992 would reflect the need to replace units that became dilapidated or went out of service for other reasons.

The big player needed to push the economy forward is the consumer. Here's the perceived rub: If consumers are to spend and thus bolster business confidence, they need money, which means they need jobs, which means businesses must hire, which they are afraid to do because they are pessimistic, so consumers won't have the money to spend to make business more optimistic. Consumers, however, have actually been doing their darndest to help out by spending nearly every cent they've earned. (That's dangerous in the long run because the economy needs savings to plow into plant and equipment, but right now we're in a difficult short run.) As a result, consumer spending has risen at a respectable 3% inflation-adjusted rate since last winter. Consumers, meanwhile, have been paring the huge debt they piled up in the 1980s, which means that 3% growth in spending is sustainable. But it's going to take some time before continued—albeit unexciting and often halting—consumer spending prompts business executives to lift their hiring plans.

Another fairly positive sign: Executives seem willing to invest in equipment. Since plunging in 1991's first quarter, business purchases of capital equipment have rebounded nicely. The catch is that the rebound is not widespread—it's been concentrated in computers and commercial aircraft. Investment in industrial equipment has declined in recent quarters; as of the third quarter of 1991, it was down 12% from a year earlier. Look for computers and aircraft to continue upward in 1992. Technological advances and productivity enhancement drive computer purchases. Commercial aircraft backlogs are bound to descend from their lofty heights, but deliveries will grow, reflecting the mass of orders placed in the last five years. Demand for industrial equipment should turn around as continued consumer spending eats away at inventories and companies hike production. Industrial equipment demand will also be coming from manufacturers with good export business. The equipment side of capital investment will thus do fairly well, but still less well than in other recoveries because consumer demand will be held back by debt fears.

The other part of capital invest-



ment—nonresidential construction—will sink further. Electrical wholesalers don't have to be told about the sorry state of commercial construction. But let it be noted that the big declines foreseen after the 1986 Tax Act, which took away real estate investment tax benefits, didn't materialize for a long time. Office buildings in the pipeline kept coming to completion, adding yet more unwanted space to markets with already sky-high vacancy rates. But in the past year, the commercial building market reaped what it had sowed: Real outlays on new offices plunged nearly 30%, as did those on retail buildings; for hotels, they were down nearly 50%. The drama will subside in 1992, but the direction will be the same.

If you're looking for some nonresidential construction customers in 1992, go back to school. State and local governments raised a record sum in 1991 for capital improvements and school building. Not only is education politically popular, but the baby boomlet that began in the late 1980s is fueling the physical need for more classrooms. So ironically, governments that face tremendous fiscal crunches are spending a huge amount on construction.

Outside of construction, state and local governments will be a drag on the economy. They've already laid off thousands of workers and will likely have to lay off more. The private sector may feel it's about time that government tightened its belt—all well and good. But at the moment it means fewer people with paychecks, thus reduced demand for goods and services the private sector provides. While cutting jobs, state governments in 1991 raised taxes and fees a record $19 billion, another damper on demand. Why this big tax increase? Less revenue due to the recession and relentless spending pressure from education, Medicaid and prisons.

Federal government spending will clearly not prime the economy's pump in 1992 because in the short run the peace dividend means defense plant layoffs. Spending will also be constrained by the deficit, which hit a record $280 billion in the last fiscal year and is headed to $350 billion this year. The budget agreement struck in late 1990 caps spending growth unless new revenues are provided and requires that tax cuts be offset with spending cuts, so no net stimulus can come if the agreement stays in force. But after Harris Wofford beat Bush-proxy Richard Thornburgh in the U.S. Senate race in Pennsylvania and after New Jerseyans protested higher taxes by dumping Governor Jim Florio's Democrats, it looked more likely that the budget agreement would be deep-sixed and taxes would be cut. Still, by the time a tax plan is enacted and by the time people actually get cash in hand, much of 1992 could be history. What's more, experience shows that if taxpayers view a cut as temporary, they don't immediately go out and spend their mini-windfall. So don't let talk of tax cuts raise your assessment of business conditions in 1992.

If policy is to juice the economy, that leaves the Federal Reserve, which already has helped push interest rates down significantly in the past year. Lower rates don't seem to have helped a lot, however. If mortgage rates were the sole factor in housing, starts would be much higher than they are. Car-loan rates have come down, as have rates on home-equity loans, which can be used to finance car purchases, yet auto sales as of October were dismal. Lower rates boost bank earnings, allowing more loans. But that doesn't make a big difference if loan demand from credit-worthy borrowers is weak. The upshot: The private sector will primarily have to grind it next year, waiting for gradual improvement, despite the best intentions of the Fed.

For electrical wholesalers that means focusing business on manufacturers who export, who serve the commercial aircraft or computer markets, or who make productivity-boosting industrial equipment. To a lesser extent, look to home builders and companies that supply residential building materials, home furnishings and appliances. Private-sector nonresidential construction markets will be a disaster. But in some localities public nonresidential building will be strong.

In some localities, too, overall business will be a lot stronger than in others. The recession primarily hit the East Coast and California. In contrast, nearly every state west of the Mississippi River has enjoyed employment growth during the past year. And the Midwest has maintained its employment thanks to exports; the exception is Michigan, which depends much more on autos than do other states in the region.

The regional economic patterns established in 1990 will carry through 1992. States with lower labor and housing costs will attract businesses from higher-cost states. States bordering California, for example, have attracted both companies and individuals fleeing stratospheric housing costs and higher taxes, not to mention smog, crime and congestion.

So opportunities for individual electrical wholesalers will vary widely in 1992. Times will remain especially tough in the Northeast. But on the whole, most wholesalers can expect business to expand—albeit modestly—in 1992. □

YOUR SALES OUTLOOK

■ Predictions from the field

	1991	1992
NEW ENGLAND	**- 4.3%**	**+3.5%**
CONNECTICUT	- 6.2%	+2.9%
MAINE	S	S
MASSACHUSETTS	- 3.6%	+3.6%
NEW HAMPSHIRE	S	S
RHODE ISLAND	S	S
VERMONT	S	S
MIDDLE ATLANTIC	**- 2.5%**	**+ 6.2%**
NEW JERSEY	- 6.2%	+ 6.1%
NEW YORK	+ 0.4%	+ 5.4%
PENNSYLVANIA	- 6.5%	+ 6.7%
EAST NORTH CENTRAL	**- 0.7%**	**+ 6.9%**
ILLINOIS	+ 1.9%	+ 7.1%
INDIANA	+ 6.3%	+ 9.5%
MICHIGAN	- 5.4%	+ 7.4%
OHIO	- 1.2%	+ 5.5%
WISCONSIN	+ 3.4%	+ 7.0%
WEST NORTH CENTRAL	**+ 0.7%**	**+ 6.9%**
IOWA	+ 0.3%	+ 5.7%
KANSAS	S	S
MINNESOTA	S	S
MISSOURI	+ 1.3%	+ 8.4%
NEBRASKA	+ 0.2%	+ 5.8%
NORTH DAKOTA	S	S
SOUTH DAKOTA	S	S
SOUTH ATLANTIC	**- 7.5%**	**+ 7.3%**
DELAWARE	- 2.8%	+ 6.5%
D.C.	S	S
FLORIDA	- 7.7%	+ 7.1%
GEORGIA	- 1.7%	+10.9%
MARYLAND	-14.3%	+ 7.6%
NORTH CAROLINA	- 7.8%	+ 8.1%
SOUTH CAROLINA	- 5.6%	+ 0.9%
VIRGINIA	-13.5%	+ 8.9%
WEST VIRGINIA	- 4.9%	+ 5.3%
EAST SOUTH CENTRAL	**- 3.9%**	**+ 5.6%**
ALABAMA	- 3.7%	+ 8.2%
KENTUCKY	- 7.4%	+ 4.2%
MISSISSIPPI	- 3.2%	+ 0.9%
TENNESSEE	- 4.1%	+ 6.5%
WEST SOUTH CENTRAL	**+ 4.1%**	**+ 5.6%**
ARKANSAS	S	S
LOUISIANA	+10.1%	+ 1.1%
OKLAHOMA	S	S
TEXAS	+ 5.4%	+ 5.1%
MOUNTAIN	**+ 3.6%**	**+ 5.3%**
ARIZONA	*	+ 9.0%
COLORADO	+ 5.3%	+ 4.9%
IDAHO	+ 9.7%	+ 2.5%
MONTANA	S	S
NEVADA	- 4.3%	+ 7.7%
NEW MEXICO	S	S
UTAH	S	S
WYOMING	S	S
PACIFIC	**- 6.6%**	**+ 5.7%**
ALASKA	+12.9%	+ 7.2%
CALIFORNIA	- 7.5%	+ 8.3%
HAWAII	S	S
OREGON	- 8.1%	+ 1.6%
WASHINGTON	- 4.5%	+ 1.6%

S = Insufficient returns *Less than .1%

Based on an ELECTRICAL WHOLESALING survey of electrical distributors conducted in August 1991.